No. 21,642

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

SONORA COMMUNITY HOSPITAL, a corporation,

Petitioner

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

ON PETITION FOR REVIEW OF THE DECISION OF THE TAX COURT OF THE UNITED STATES

BRIEF FOR THE RESPONDENT

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I N D E X

CITATIONS

Cases:

Statute:

Miscellaneous:

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OPINION BELOW

The findings of fact and opinion of the Tax Court (I-R. 32-49)[1/] are reported at 46 T.C. 519.

JURISDICTION

This petition for review (I-R. 59-61) involves federal income taxes for the taxable years 1959, 1960 and 1961. On October 31, 1963, the Commissioner of Internal Revenue mailed to the taxpayer a notice of deficiency asserting deficiencies in income tax in the

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1/ "I-R." references are to volume I of the record on appeal. "II-R." references are to volume II of the record on appeal.

aggregate amount of $35,791.80. (I-R. 5-9.) Within 90 days thereafter, on January 27, 1964, the taxpayer filed a petition (I-R. 1-9) with the Tax Court for a redetermination of the deficiencies asserted for the taxable years 1959, 1960 and 1961 under the provisions of Section 6213 of the Internal Revenue Code of 1954. The decision of the Tax Court was entered on September 19, 1966. (I-R. 57-58.) This case is brought to this Court by petition for review filed on December 19, 1966 (I-R. 59-61) within the three-mont month period prescribed in Section 7483 of the Internal Revenue Code of 1954. Jurisdiction is conferred on this Court by Section 7482 of that Code.

QUESTION PRESENTED

Whether the Tax Court erred in holding that taxpayer was not operated exclusively for charitable purposes and consequently failed to qualify for exemption from income tax under Section 501(c)(3) of the 1954 Code.

STATUTE AND REGULATIONS INVOLVED

Internal Revenue Code of 1954:

> SEC. 501. EXEMPTION FROM TAX ON CORPORATIONS, CERTAIN TRUSTS, ETC.
>
> * * *
>
> (c) List of Exempt Organizations.--The following organizations are referred to in subsection (a):
>
> * * *
>
> (3) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or for the

prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

* * *

(26 U.S.C. 1964 ed., Sec. 501.)

Treasury Regulations on Income Tax (1954 Code):

§ 1.501(c)(3)-1 Organizations organized and operated for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or for the prevention of cruelty to children or animals.

* * *

(c) Operational test--(1) Primary activities. An organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

* * *

(26 C.F.R., Sec. 1.501(c)(3)-1.)

STATEMENT

The facts as stipulated by the parties and as found by the Tax Court (I-R. 33-44) may be stated as follows:

Taxpayer is a corporation organized on or about March 21, 1958, under the laws of the State of California. During the periods here at issue, taxpayer was engaged in the business of owning and operating a 42-bed general hospital at One South Forest Road, Sonora, California. For federal income tax purposes, taxpayer filed a Return of Organization Exempt From Income Tax (Form 990-A) for each of its fiscal years ending March 31, 1959, 1960 and 1961, with the District Director of Internal Revenue at San Francisco, California. (I-R. 33.)

In 1950, Ben R. Boice, a medical doctor, established a medical practice in Sonora, a town of about 2,500 inhabitants which serves a county (Tuolumne) having a population of about 18,000. He became a member of the staff at the Columbia Way Hospital in Sonora. There were then two other hospitals in the town, the Sonora Hospital and the Tuolumne County Hospital. Dr. Boice had a "sort of a courtesy staff membership" at the Sonora Hospital, but none at the County Hospital. The Sonora Hospital was housed in a small, old building, having 13 beds. It was located on Washington Street, the main street in Sonora. Its owner, Dr. Wrigley, died around 1950, and it was thereafter closed as a hospital. Dr. Boice purchased the property from Dr. Wrigley's widow in 1953 for use as an office. (I-R. 33-34.)

Paul L. Anspach is a medical doctor who had come to Sonora shortly before 1954. In January, 1954, he and Dr. Boice formed a partnership to practice medicine in Sonora. The partnership offices were located on the main floor of the old Sonora Hospital building which, as noted above, had been purchased by Dr. Boice; the upper floor was shut off and the bottom floor was used for storage. (I-R. 34.)

At some time prior to 1956, Drs. Boice and Anspach began to have difficulties with the Columbia Way Hospital and they were "virtually tossed out of" that hospital. In order to continue to practice medicine in Sonora it became imperative for them to obtain some other hospital connection. Accordingly, in January, 1956, they reopened and began to operate the old Sonora Hospital. They increased its capacity to 21 beds. It was their intention at that time to build a more adequate and modern hospital facility in Sonora. The State of California issued a temporary one year permit to Drs. Boice and Anspach to reopen and operate the old Sonora Hospital, pending completion of a new hospital, and they operated the hospital as a partnership under the name "Sonora Hospital". (I-R. 34-35.)

Drs. Boice and Anspach attempted unsuccessfully to interest various persons and organizations in undertaking the building, financing and operation of a new community hospital in Sonora. However, they were able to obtain on their own behalf a loan of $200,000 from the Small Business Administration of the United States and with this money, and additional sums advanced by them as individuals, they purchased a parcel of realty located at

One South Forest Road in Sonora and constructed a 42-bed hospital thereon. This hospital was completed on July 7, 1957. (I-R. 35.)

Upon completion of the new hospital at One South Forest Road, Drs. Boice and Anspach closed their hospital operation at Washington Street and moved it to the new location. However, at that time they continued to maintain their office in the old Sonora Hospital building. In 1959, they placed a new building adjacent to the hospital building at One South Forest Road and moved their offices into this new building. (I-R. 35.)

On January 9, 1956, at about the time the old Sonora Hospital was reopened, Drs. Boice and Anspach entered into an agreement with two brothers, Jack and James C. Rucker, both of whom are registered "technologists", whereby the Ruckers were to operate laboratory and X-ray facilities at the Sonora Hospital or such other hospitals as might be established by Drs. Boice and Anspach during the term of the agreement, which was to be ten years. (I-R. 35-36.)

The January 9, 1956 agreement provided that the Ruckers were to establish, equip, staff, and maintain laboratory and X-ray facilities in quarters provided in the hospital by Drs. Boice and Anspach. Further, Drs. Boice and Anspach were to make use of the laboratory and X-ray facilities so established exclusively for all laboratory and X-ray work required by them in their practice or in connection with the operation of the hospital. Also, Drs. Boice and Anspach were to bill and collect all charges in

respect of laboratory and X-ray work on in-patients and remit these collections to the Ruckers. Work on out-patients was to be billed directly by the Ruckers. In consideration for the above, the Ruckers agreed to pay to Drs. Boice and Anspach one-third of the total gross receipts derived from the operation of the laboratory and X-ray departments. The doctors were not required to perform any services under the terms of the agreement with respect to the operation of either the laboratory or the X-ray department. (I-R. 36.)

Pursuant to the agreement of January 9, 1956, the Ruckers operated the two departments, namely, the laboratory and the X-ray facility, as a separate trade or business in partnership form under the name of Sonora Hospital Laboratory and X-ray Company. The services thus rendered consisted of the operation of a general X-ray department and a clinical laboratory; the work of the laboratory involved making blood counts, cholesterol counts, urinalyses, etc. However, neither the Sonora Hospital Laboratory and X-ray Company, nor Drs. Boice and Anspach made pathological examinations of tissue; such work was sent out to a pathologist. (I-R. 36-37.)

Upon moving into the new hospital on July 7, 1957, Drs. Boice and Anspach assigned approximately 1,000 square feet of floor space in the new building to the Ruckers for installation of their laboratory and X-ray equipment. The Ruckers moved into the new building and continued performing in accordance with the January 9,

1956 agreement. At this time, the Ruckers completely re-equipped the laboratory and X-ray facilities at their own expense. (I-R. 37.)

On or about March 21, 1958, Drs. Boice and Anspach caused the incorporation of taxpayer under the name of Boice-Anspach Foundation, pursuant to the General Non-Profit Corporation Law, Part 1 of Division 2 of Title 1 of the Corporation Code of the State of California. Subsequently, on or about June 11, 1958, taxpayer changed its name to Sonora Community Hospital. (I-R. 37.)

On or about March 31, 1958, Drs. Boice and Anspach sold their partnership interests in the hospital located at One South Forest Road to taxpayer for a net consideration of approximately $251,180. In consideration for these assets, taxpayer gave Drs. Boice and Anspach 20 promissory notes bearing interest at six percent and payable over a period of years beginning in 1968. (I-R. 37-38.)

Subsequent to the transfer of the hospital to taxpayer the Ruckers continued to operate the laboratory and X-ray departments in the same fashion as when the doctors owned the hospital. Up until about May 26, 1958, they continued to remit one-third of the gross receipts derived from the operation of these facilities directly to Drs. Boice and Anspach. On or about May 26, 1958, Drs. Boice and Anspach directed the Ruckers to pay the one-third share of the gross receipts to Leasing Company of Sonora, a corporation wholly owned by these doctors. They had caused it to

be incorporated about December 2, 1957, and were its sole stockholders at all times pertinent. (I-R. 38.)

The Ruckers complied with this directive. Leasing Company of Sonora did not rent any equipment or property to either taxpayer or Sonora Hospital Laboratory and X-ray Company. About two-thirds of all the fees collected were attributable to the operation of the X-ray department and the remaining one-third to the laboratory. (I-R. 38.)

In October, 1959, Drs. Boice and Anspach directed the Ruckers to pay taxpayer $100 per month out of their one-third share of the gross receipts derived from the laboratory and X-ray facilities and to continue to pay the balance of that share to Leasing Company of Sonora. In May, 1960, Drs. Boice and Anspach directed the Ruckers to pay the entire one-third share to taxpayer. (I-R. 38.)

The Sonora Hospital Laboratory and X-ray Company billings and payments for both out-patients and in-patients for the calendar years 1958, 1959, 1960, and the period January 1, 1961 through September 30, 1961 were as follows (I-R. 39):

	Billings		Payments	
	Out-Patients	In-Patients	Out-Patients	In-Patients
1958	$37,482.84	$47,903.63	$35,139.24	$43,237.15
1959	39,308.72	51,121.66	36,453.46	38,382.98
1960	48,885.60	52,747.75	43,114.36	42,580.19
1/1/61-9/30/61	38,382.98	33,158.22	34,374.72	42,795.99

During taxpayer's fiscal years ended March 31, 1959, 1960 and 1961, the Ruckers paid $25,121.07, $23,135.82, and $1,898.32, respectively, to Leasing Company of Sonora as directed by Drs. Boice and Anspach. Leasing Company of Sonora used these monies to make investments not related in any way to taxpayer's operations. (I-R. 39.)

During the years here in issue, the State of California had no licensing provisions concerning X-ray technicians or the operation of X-ray equipment, and the Ruckers were empowered under California law to operate and in fact did operate the X-ray department in the hospital without any supervision by a physician. Although an X-ray department in a hospital is usually under the supervision of a radiologist (a physician who specializes in the interpretation of X-ray films and in the performance of fluoroscopic examinations) or other qualified medical doctor, neither Dr. Boice nor Dr. Anspach in fact supervised that department. Neither was a radiologist. Each would perform fluoroscopic examinations of his own patients and each would examine X-ray films taken by the Ruckers of his own patients, but such examinations were merely those which any physician might make in respect of his own patients who were sent to the X-ray department, rather than those which would be made by the director or other qualified supervising physicia in the X-ray department. In 1961, taxpayer hired a qualified radiologist, Dr. Robert Powell, to take charge of the radio-

logical services. He performed fluoroscopy work and reviewed X-rays taken in his department, submitting a written report to the attending physician. His work in that respect differed markedly from the examinations that Drs. Boice and Anspach might make in respect of their own patients or in connection with an occasional case in which some other physician might solicit their opinion in respect of a particular patient. Neither Dr. Boice nor Dr. Anspach rendered compensable services in the X-ray department as director or otherwise; any services performed by either of them in relation to X-rays were those that might be rendered by any practicing physician unconnected with the operation of the X-ray department. (I-R. 39-40.)

The situation in respect of the laboratory was somewhat different from that of the X-ray department. California law required that the laboratory be "under the direct and responsible supervision and direction of" a licensed clinical laboratory bioanalyst or a licensed physician and surgeon. Section 1284, California Business and Professions Code. Since neither of the Ruckers qualified under either of these categories, Dr. Boice signed the required application for the license to operate the laboratory, and became in name the director of the laboratory. Dr. Boice continued in this capacity from January 9, 1956 until sometime in 1959. However, all work in the laboratory was done by the Ruckers or under their supervision. (I-R. 40-41.)

Under Section 1285 of the California Business and Professions Code it "is unlawful for a licensed * * * physician and surgeon to serve only as the nominal director or supervisor of a clinical

laboratory." Although reports issued by the laboratory were signed in Dr. Boice's name, there is no convincing evidence in this record that he actually supervised or directed the operation of the laboratory to any appreciable extent, if at all. Nor does it appear that Dr. Anspach ever acted as director of the laboratory either in fact or nominally. To the extent that Dr. Boice might have questioned the results of any tests performed by the laboratory in respect of any of his patients and required the tests to be repeated, the situation was no different from that of any physician who might have sent his patients to the laboratory for tests; such action by him did not in any manner represent the supervision or direction of the operation of the laboratory. In 1959, Dr. Theodore C. Howard, an employee of Drs. Boice and Anspach, signed the license application as director of the laboratory. Although the medical director of a clinical laboratory is often a physician specializing in pathology, and may receive between 30 and 40 percent of the gross receipts of the laboratory, it does not appear that either Dr. Boice or Dr. Howard had any special qualifications as a pathologist or that Dr. Howard was in fact any more active than Dr. Boice in the actual operation or supervision of the laboratory. (I-R. 41-42.)

There were several other doctors associated with Drs. Boice and Anspach in the practice of medicine; they all occupied the same offices and all of them are sometimes referred to herein in

the aggregate as the "medical group". There were about ten doctors in Sonora when taxpayer acquired the hospital from Drs. Boice and Anspach. Seven of them were on the hospital staff, and four of the seven were members of the medical group. At the time of trial herein (January 1966) there were about fifteen doctors in Sonora, eleven of whom were on the hospital staff and five in the medical group. About 90 per cent of taxpayer's patients were patients of members of the medical group. (I-R. 42.)

Dr. Anspach's wife, Helen, is a physician, and during the tax years served as administrator of the hospital without compensation. Drs. Boice and Anspach also performed various administrative services in the operation of the hospital for which they were not compensated. (I-R. 42-43.)

Taxpayer had no endowment and no source of income other than the fees received for services rendered to patients. It had no written rules or regulations regarding the admission of charity patients, and it did not ordinarily admit charity patients. Its practice was to refer charity patients to the County Hospital, and on occasion when a charity patient was admitted in an emergency it would have him transferred when circumstances permitted to the County Hospital. It did admit and retain charity patients in a small number of instances. The total amount of free care furnished was less than one percent of paid care. In some instances patients were admitted with the understanding that they

would pay less than the full regular charges--usually to the extent that hospital insurance or some other similar plan covered the services involved. Unpaid patient accounts were turned over to a collection agency, including amounts part-pay patients had agreed to pay. During the period March, 1959 to January 1, 1961, taxpayer turned over $34,721.72 of unpaid patient accounts for collection. (I-R. 43.)

On or about August 14, 1959, taxpayer filed an exemption application with the Commissioner, requesting exemption from federal income taxes as a corporation organized and operated exclusively for charitable purposes within the meaning of Section 501(a) and 501(c)(3) of the Internal Revenue Code of 1954. (I-R. 43-44.)

On this application form, and in its subsequent correspondence with the Commissioner concerning the application, taxpayer made no mention of the participation by Drs. Boice and Anspach in the gross receipts derived from the laboratory and X-ray operations conducted on its premises. (I-R. 44.)

On February 29, 1960, the Commissioner ruled that taxpayer was exempt as an organization described in Section 501(c)(3) of the Internal Revenue Code of 1954 on the basis that taxpayer had shown that it was organized and operated exclusively for charitable purposes. This ruling was made effective beginning April 1, 1958.

On December 26, 1962, the Commissioner revoked this ruling of February 29, 1960. (I-R. 44.)

In 1961, after the last of the three fiscal tax yesrs involved herein, the articles of incorporation and bylaws of taxpayer were completely amended and it became an integrated institution wholly operated by the Seventh-day Adventist Church. In connection with the absorption of the hospital by the Church, Drs. Boice and Anspach forgave payment on the notes (including all accrued interest) which they had received upon transferring the hospital assets to taxpayer. (I-R. 44.)

The Tax Court upheld the Commissioner's retroactive revocation, holding that the taxpayer was not a charitable corporation exempt from tax under Section 501(c)(3) on the ground that it was not operated exclusively for charitable purposes. (I-R. 14-15, 18.)

From that action, the taxpayer has filed and prosecuted the instant petition for review.

SUMMARY OF ARGUMENT

Taxpayer, a hospital, claimed exemption from income tax as a charitable corporation for the taxable years in issue (1959-1961). Pursuant to Section 501(c)(3) of the 1954 Code, taxpayer was required to show, among other things, that it was operated exclusively for charitable purposes. The record developed in the Tax Court, however, indicated that taxpayer's charitable activities were insubstantial while its operations benefited to a substantial extent the private interests of the two medical doctors who were its founders. Accordingly, the Tax Court, viewing the picture whole, inferred from what taxpayer actually did that its operation was not exclusively for charitable purposes and that its claim for exemption consequently should be denied.

On this appeal, the strategy of taxpayer is to isolate each element considered material by the Tax Court and to attempt a demonstration that any one of them, standing alone, would not justify denial of exempt status. A principal difficulty confronting taxpayer is that the Supreme Court has interpreted the word "exclusively" in a similar context to mean that a single nonexempt purpose, if substantial in nature, destroys the claim to exemption. It follows that the Section 501(c)(3) requirement of operation for exclusively charitable purposes requires a balancing of the charitable aspects of the operation against any private benefit in a factual inquiry as to what the taxpayer's real purposes are. No single element need be determinative. The ultimate inference drawn by the Tax Court has a rational

foundation in its subsidiary findings, all of which are supported by substantial evidence, representing, in some cases, its resolution of conflicts in the testimony.

The decision of the Tax Court is correct and should be affirmed.

ARGUMENT

THE TAXPAYER DID NOT QUALIFY AS AN EXEMPT CHARITABLE CORPORATION UNDER SECTION 501 (c)(3) OF THE 1954 CODE BECAUSE IT WAS NOT OPERATED EXCLUSIVELY FOR CHARITABLE PURPOSES

The taxpayer in this case claims to be a charitable corporation exempt from tax during the years in issue under Section 501(c)(3) of the Internal Revenue Code of 1954, supra. A corporation is entitled to be exempt from tax under Section 501(c)(3) if it meets the following requirements: (1) it must be organized and operated exclusively for charitable purposes; (2) no part of its net income may inure to the benefit of a private individual or shareholder; (3) it cannot engage in substantial political or lobbying activities.

The sole question presented by this appeal is whether the Tax Court correctly determined that the taxpayer was not entitled to tax-exempt status under Section 501(c)(3) on the ground that it was not operated exclusively for charitable purposes. The Treasury Regulations under Section 501(c)(3)[2/] set forth an "operational test" for the purpose of determining whether a corporation claiming a tax-exempt status is being operated exclusively for the exempt

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2/ Treasury Regulations on Income Tax (1954 Code), Section 1.501(c)(3)-1(c)(1), supra.

purpose. Under those Regulations, a corporation claiming to be operated exclusively for an exempt purpose must be engaged primarily in activities which accomplish that purpose and not more than an insubstantial amount of its activities may be in furtherance of nonexempt purposes. Treasury Regulations on Income Tax (1954 Code), Section 1.501(c)(3)-1(c)(1), supra. These requirements are merely declaratory of existing case law interpreting the term "operated exclusively" as used in Section 501(c)(3). Stevens Bros. Foundation, Inc. v. Commissioner, 324 F. 2d 633 (C.A. 8th), certiorari denied, 376 U.S. 969; Duffy v. Birmingham, 190 F. 2d 738 (C.A. 8th). See also Better Business Bureau v. United States, 326 U.S. 279, and United States v. Fort Worth Club, 345 F. 2d 52 (C.A. 5th), modified and reaffirmed per curiam, 348 F. 2d 891. Although the Better Business Bureau case involved an exemption from social security taxes, the language of the exempting clause was similar to Section 501(c)(3). In the oft-quoted words of that opinion (p. 283), "This ["exclusively"] plainly means that the presence of a single noneducational purpose, if substantial in nature, will destroy the exemption * * *".

The essentially factual inference drawn by the Tax Court -- that taxpayer was not operated exclusively for exempt purposes -- is supported not only by the evidence that taxpayer's charitable activities were insubstantial, but also by the evidence that in some respects it served the private interests of the two medical doctors who were its founders. The method of the Tax Court here was to balance all of these aspects against each other to arrive

at an overall picture of the operational purposes of taxpayer. Although taxpayer attempts, on this appeal, to isolate each aspect of the elements deemed material by the Tax Court and argues that any one of them, standing alone, does not bar exempt status, it should be clear that the Tax Court's approach is necessitated by the terms of Section 501(c)(3).

Turning first to taxpayer's claimed public purpose, the evidence shows only an insubstantial amount of charitable activity. Taxpayer never in fact held itself out as a charitable organization. It had no rules or regulations or any other printed material setting forth charitable programs or policies. (II-R. 57-58.) Moreover, one of the taxpayer's founders testified that the taxpayer usually refused patients without funds, referring them to the County Hospital. (II-R. 58, 59-60, 115.) While the founder testified that some patients were admitted for reduced rates, he admitted that less than one percent of the care furnished by the taxpayer was without charge. (II-R. 60.) Assuredly, the charity record of a charitable hospital may be low, depending upon all the facts. Cf. Commissioner v. Battle Creek, 126 F. 2d 405 (C.A. 5th); Rev. Rul. 56-185, 1956-1 Cum. Bull. 202. The charitable activities must, however, rise above the de minimis level. Cf. Lorain Avenue Clinic v. Commissioner, 31 T.C. 141, 161; Duffy v. Birmingham, supra; Stevens Bros. Foundation, Inc. v. Commissioner, supra. Since the charitable activities of the taxpayer here did not arise above that level it is clear that the taxpayer was not engaged primarily in activities which accomplish the claimed charitable

purposes as is required under the "operational test" set forth in the Regulations.

Viewed from the other end, it appears that taxpayer's operation substantially benefited its founders, who were able to send their patients there after losing their connection with the Columbia Way Hospital. (I-R. 34-35.) More graphically, the two founding medical doctors allocated 1,000 square feet of space in the Sonora Hospital building (owned by the taxpayer) to two private individuals for the purpose of operating an X-ray department and clinical laboratory. (I-R. 37.) The founders had an agreement with these individuals whereby the former would receive one-third of the gross receipts of the X-ray department and clinical laboratory. (I-R. 36, 47-48.) During the years in issue, the proprietors of the X-ray department and laboratory, pursuant to this arrangement paid the founders of the taxpayer approximately $50,000.[3/] (I-R. 39.) Taxpayer argues (Br. 8-12) that the founding doctors actually performed valuable services for which they received the amounts in question. However, as noted by the Tax Court, this is not borne out in the record. (II-R. 36, 50, 85-86, 120, 122, 164-167.)

The Tax Court stated in this regard (I-R. 48-49):

> Petitioner attempts to justify the arrangement on the ground that the one-third gross receipts thus paid over were for services rendered. The answer, however, is simple, namely, that the contract between Drs. Boice and Anspach and the Ruckers did not call for the performance of any services by the doctors,

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3/ Technically this amount was paid to the Leasing Company of Sonora; however, this corporation was wholly owned by the founders of the taxpayer. (I-R. 38.)

> and in any event, we do not believe that any services of consequence were rendered calling for payments in the amounts involved. Certainly, in respect of the X-ray department, which accounted for about two-thirds of the receipts, we cannot find on this record that prior to the advent of Dr. Powell in 1961 either Dr. Boice or anyone associated with him rendered any services of consequence to that department. * * * And even as to the clinical laboratory, the evidence convincingly indicates that Dr. Boice, and later Dr. Howard, served merely as the nominal director without any actual supervision over its activities. Although the burden was upon petitioner, the questioning of Dr. Boice in an effort to pinpoint just what he did in relation to the laboratory brought forth no clear answers showing any real supervision over the laboratory.

The insubstantial nature of the charitable activities of the hospital operated by the taxpayer, coupled with the undeniable private benefits to its founders, are sufficient to support the Tax Court's inference that taxpayer was not operated exclusively for charitable purposes within the meaning of Section 501(c)(3). 4/

4/ The Tax Court reserved judgment on the question of whether the substantial and recurring amounts received by taxpayer's founders during the years in issue amounted, in substance, to "rent" which taxpayer should have received for its space occupied by the X-ray operation and clinical laboratory (I-R. 47) and whether some part of taxpayer's net earnings inured to the benefit of its founders. If that view had been taken by the Tax Court -- and this record fully supports the conclusion that at least part of such amounts was "rent" -- then taxpayer would be disqualified by the requirement of Section 501(c)(3) that "no part of the net earnings * * * inures to the benefit of any private shareholder or individual." The earnings of a corporation may inure to the benefit of a private individual in an indirect as well as in a direct manner. See Horace Heidt Foundation v. United States, 170 F. Supp. 634 (Ct. Cl.); Wells & Wade, Inc. v. United States, 280 F. 2d 825 (Ct. Cl.); Northwestern Municipal Assn. v. United States, 99 F. 2d 460 (C.A. 8th).

Accordingly, the Tax Court's determination that the taxpayer was not entitled to exemption from income tax under Section 501 (c)(3) similarly is correct.

CONCLUSION

For the reasons stated, the decision of the Tax Court is correct and should be affirmed.

Respectfully submitted,

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APRIL, 1968.

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

Dated: _____ day of _____, 1968.

_____
Attorney